Mortgage escrow accounts have been in the news lately and seem to be greatly misunderstood by many consumers. The original idea behind escrow accounts was to protect the interests of homeowners, and they have been serving that purpose for more than 50 years.

THE HISTORY OF ESCROWS

Mortgage escrow accounts came into being more than 50 years ago. In the 1930's, many Americans were losing their homes in foreclosures because of late tax payments. To help ease the burden on homeowners who had to come up with large, lump sum payments at tax time, lenders agreed to take on the responsibility by collecting smaller monthly sums from homeowners along with their mortgage payment. In 1934, the government mandated that lenders manage escrow accounts on all FHA insured mortgages. This then became the standard practice for all mortgages.

WHY MORTGAGE ESCROWS?

Mortgage escrow accounts ensure that homeowners' property taxes, fire and hazard insurance premiums, mortgage insurance premiums, and other escrow items are paid in a timely fashion. They are a guarantee that there is always enough money to pay these bills when they are due, so that the homeowner avoids the risk of lapsed insurance coverage or delinquent taxes.

WHO'S PROTECTING THE HOMEOWNER?

Escrowing is governed by the Real Estate Settlement Procedures Act of 1974 (RESPA.), administered by the U.S. Department of Housing and Urban Development (HUD), HUD Building Washington DC 20410, 202-708-0926. Lenders must manage their escrow accounts in compliance with this federal law and with the interpretations set out by HUD.

In addition, the 1990 Housing Bill signed into law by the President, requires lenders to issue itemized statements of escrow accounts to borrowers on an annual basis. While many lenders are already providing homeowners with regular statements of their escrow accounts, the new law should ensure that every lender follows this practice.

WHAT ESCROWS DO FOR HOME BUYERS

Guarantee that bills are paid on time. The most obvious advantage of escrows is that they automatically budget the borrower's tax and insurance responsibilities over the course of a year. Homeowners do not have to worry about coming up with several large, lump sum payments, each with different due dates, throughout the year. If there is ever a fire in the home, or if the basement floods causing damage, the homeowner is assured that the home is protected by up-to-date insurance.

Unexpected increases are taken care of. Because of escrows, homeowners also do not need to worry about calculating unexpected increases in their taxes or insurance premiums. It is the responsibility of the lender to allow for possible increases in these payments.

Even when there are not enough funds in a mortgage escrow account to meet increased tax or insurance payments, the lender typically covers the bill without charging interest to the borrower. It is very common for lenders to pay taxes and insurance premiums when they are due, even though all the money for these bills has not yet been collected from the homeowner. Lenders advanced more than $600 million to homeowners, who then avoided the penalties and risks of not paying their taxes and insurance on time.

Mortgages have lower rates and down payments because of escrows. Escrows protect the interests of investors in home mortgage loans. By making home mortgages more attractive and secure as investments, escrowing has led to a healthier mortgage market. As a result, loans with better terms and lower down payments are available to homebuyers.

Local governments save money. Escrow accounts also benefit local governments by providing a more efficient, less expensive means of tax collection. Rather than working with millions of homeowners, municipalities need only collect from a few hundred lenders.

HOW DOES THE LENDER COME UP WITH MY PAYMENT?

The law is very specific in setting limits on the amount that the lender may collect. The lender may require a monthly payment of 1/12 of the total amount of estimated taxes, insurance premiums, and other charges reasonably anticipated to be paid. In addition, the lender may collect an additional balance of not more than 1/6 of the estimated annual payments. If the lender determines there will be or is a deficiency in the escrow accounts, the law permits the lender to require additional monthly deposits to avoid or eliminate the deficiency.

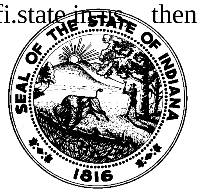
WHAT HAPPENS WHEN MY LOAN IS TRANSFERRED?

When the servicing of your loan is transferred to another lender, the new lender takes on the responsibility of managing your escrow account. At that time, the new lender may examine your escrow account to make sure that the funds being collected are sufficient to cover all payments that are to be made. If the new lender feels that the amount collected must be adjusted, you will be notified of the change in your monthly payment.

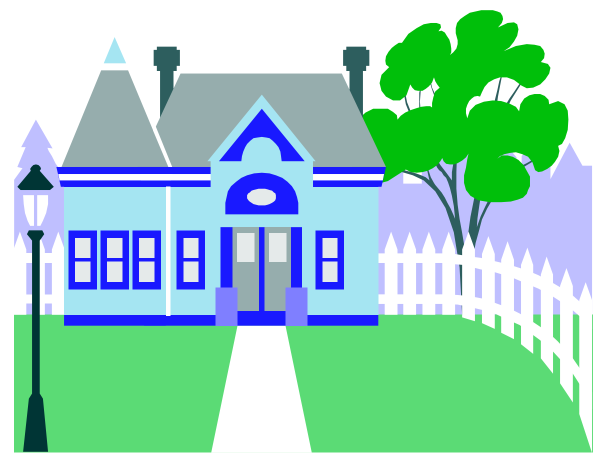
The Indiana Department of Financial Institutions, Division of Consumer Credit has many other credit related brochures available, such as:

- Answers to Credit Problems
- Applying for Credit
- At Home Shopping Rights
- Bankruptcy Facts
- Buried in Debt
- Car Financing Scams
- Charge Card Fraud
- Choosing A Credit Card
- Co-Signing
- Credit and Divorce
- Credit and Older Consumers
- Deep in Debt?
- Equal Credit Opportunity
- Fair Credit Reporting
- Fair Debt Collection
- Gold Cards
- Hang up on Fraud
- High Rate Mortgages
- Home Equity Credit Lines
- How to Avoid Bankruptcy
- Indiana Uniform Consumer Credit Code
- Look Before you Lease
- Mortgage Loans
- Repossession
- Reverse Mortgage Loans
- Rule of 78s – What is it?
- Scoring for Credit
- Shopping for Credit
- Using Credit Cards
- Variable Rate Credit
- What is a Budget?
- What is the DFI?

Call our toll-free number or write to the address on the cover for a copy of any of the brochures listed or for further consumer credit information. You can also access information at our web site on the Internet: http://www.dfi.state.in.us then click on Consumer Credit.



MORTGAGE ESCROW ACCOUNTS



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